


Utah Governor's Office *of* Economic Development

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Financing Export Transactions

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Partnerships for International Development

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UTAH WORLD TRADE CENTER

U.S. COMMERCIAL SERVICE

United States of America Department of Commerce

DISTRICT EXPORT COUNCIL

Introduction

1. **Export finance is a specific topic in financial industry.**

- Product sold & shipped overseas = takes longer to get paid.
- Thorough due diligence & financial management necessary to ensure that buyers are reliable and creditworthy.
- Goal:
  i. avoid common mistakes
     a) securing the wrong type of financing
     b) miscalculating the amount your company needs to finance
     c) underestimating the cost of borrowing the money

Introduction

2. **Flexible payment terms have become a fundamental part of any sales package:**

   – Selling on open account,: places all of the risk with the seller.

   – Cash-in-advance terms: place all of the risk with the buyer.

   – Trade finance:

   i. Pre-shipment financing to produce or purchase the material and labor necessary to fulfill the sales order; or

   ii. Post-shipment financing to generate immediate cash while offering payment terms to buyers.

3. **In our experience, if your competitor sells a similar quality product and *provides financing* or better payment terms, you have probably lost a sale.**

General Considerations

1. As an exporter you may need financing:
   - to produce the goods
   - finance other aspects of a sale (e.g. promotion and selling costs)
   - engineering modifications
   - shipping costs

2. Financing Costs:
   - The costs of borrowing (e.g. interest rates, insurance, fees) will vary
   - Understand total cost and its effect on pricing and profit before sending pro forma invoice to the buyer.

3. Financing Terms:
   - Costs increase with length of terms
   - Be aware of impact on pricing and profit

General Considerations

4. Risk Management:

   – Greater risks = greater cost (e.g. political and currency stability; creditworthiness of buyer)

5. Lender concerns:
   – Exporter performance: the exporter can produce and ship the product on time, and the product will be accepted by the buyer.
   – Buyer performance: buyer is reliable with a good credit history. Lenders evaluate any commercial or political risk.
   – Additional credit capacity may be needed if criteria is not met: government guarantee programs are available that may enable the lender to provide additional financing.

Types of Trade Finance

- Working capital loans
  1. Generally associated with pre-shipment financing: covers operating costs related to a sales or contract.
  2. Loan proceeds usually finance the following areas:
     – Labor
     – Materials
     – Inventory
- Term financing for foreign buyers
  1. Foreign buyers usually want some form of financing for major purchases.
  2. Few exporters can handle the cash flow issues of financing the sale and may be unwilling to bear the risks involved in a foreign transaction.
  3. Buyer credit programs offer a potential solution: provides loan guarantees to commercial lenders. Buyers get extended terms.

Trade Finance Products

- Factoring: a financial transaction whereby a business sells its accounts receivable (i.e., invoices) to a third party (called a factor) at a discount in exchange for immediate money with which to finance continued business.

  – Factoring differs from a bank loan in three main ways:

    1. First, the emphasis is on the value of the receivables (essentially a financial asset), not the firm's credit worthiness.
    2. Secondly, factoring is not a loan (sometimes confused with invoice discounting) – it is the purchase of a financial asset (the receivables account).

  – Factors typically provide 70% of the face value of the A/R and assumes liability for collection. Once final payment is received, the factor pays the buyer the remaining 30% minus a 4-5% service fee.

Trade Finance Products

- **Forfaiting: involves the purchasing of receivables from exporters. In factoring, a firm sells all its receivables while in forfaiting, the firm sells one of its transactions.**
- **The characteristics of a forfaiting transaction are:**
  - Credit is extended to the exporter for a period ranging between 180 days to seven years.
  - Minimum bill size is normally US$ 250,000, although $500,000 is preferred.
  - The payment is normally receivable in any major convertible currency.
  - A letter of credit or a guarantee is made by a bank, usually in the importer's country.
  - The contract can be for either goods or for services.
- **Three elements relate to the pricing of a forfaiting transaction:**
  - Discount (interest) rate usually quoted as a margin over LIBOR.
  - Days of grace, added to the actual number of days until maturity for the purpose of covering the number of days normally experienced in the transfer of payment, applicable to the country of risk.
  - Commitment fee, applied from the date the forfaiter is committed to undertake the financing, until the date of discounting.

Trade Finance Products

- **Purchase Order Financing:** short-term technique where money is advanced against a purchase order for finished goods or value added products to finance the manufacturing of the item.
  - Cash flow during manufacturing process can be an issue for suppliers, particularly if the order is for a particularly large amounts of goods. In order to obtain short term financing for raw materials, labor, etc., the supplier may finance the financial needs of the manufacturing process using the P.O. and inventory as collateral.
  - One key element is that the customer must be creditworthy.
  - Risky (e.g. customer could reject order, untimely delivery, etc.) so it is more expensive.
  - Extensive due diligence is required and lenders are highly selective.

Sources of Export Financing

- Commercial Banks
  - commercial bank with an international department.
  - familiar with export business and provides international banking services related to documentary collections and letters of credit, including the discounting of drafts.
  - The responsibility for repaying a working capital loan ordinarily rests with the exporter, even if the foreign buyer fails to pay.
    1. **The bank takes this contingency into account in deciding on an export working capital line of credit.**
    2. **It is to the benefit of the bank and the exporter to improve the quality of the export receivables by using letters of credit and by making use of credit insurance, or by using Export-Import Bank or Small Business Administration working capital guarantees.**
- Government Assistance Programs
  - **Export-Import Bank (Ex-Im Bank) is the federal government's trade finance agency, offering numerous programs to address a broad range of needs and small and medium-sized exporters**.

Sources of Export Financing

- Ex-Im bank credit insurance protects against default on exports sold under short-term credit. Other guarantee and loan programs extend medium and long-term credit for durable goods.
- Other government agencies:
  - **The Small Business Administration (SBA) offers programs to address the needs of smaller exporters.**
  - **U.S. Department of Agriculture offers several medium- and long-term credit programs to foster agricultural exports.**
  - **OPIC provides specialized assistance to U.S. firms through its performance bond and contractor insurance programs for U.S. investments abroad that also can be accessed by U.S. exporters.**
  - **The Trade Development Administration provides grants for project planning activities conducted by U.S. firms and thereby seeks to give a U.S. imprint on project feasibility studies and design.**
  - **The Agency for International Development (AID) provides grants to developing nations that can be used to purchase U.S. goods and services.**

UPCOMING SEMINARS

- September 22 - Business Travel Orientation
- October 20 - After Sale Service
- November 17 - How to Use the Automated Export Service (AES)

STAFF

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Thank you for your participation.